

## ***Doing Business in China: Methods of Payment and Financing***



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### ***Chindex International, Inc.***

#### **Capital Medical Equipment**

##### **US\$ Sales to Hospitals**

- direct sales force for top quality imported products
- largest independent U.S. distributor since 1981

#### **Healthcare Products Distribution**

##### **Local Currency Sales/Logistics Platform**

- dealer sales of low-cost instrumentation and consumables
- retail pharmacy distribution network

#### **Healthcare Services**

##### **United Family Hospitals & Clinics Network**

- Beijing United Family Hospital & Clinics -- 1997
- Shanghai United Family Hospital & Clinics -- Late 2003



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### ***How Healthcare Products are Distributed in China***

#### **1. Capital Equipment Exported to China**

- US\$-denominated sales to hospitals (via FTCs)

#### **2. Consumable Products Imported into China**

- RMB-denominated sales to local Chinese dealers



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## Capital Equipment Exports - Traditional Distribution Structure

- **Representative Office Operations**
  - Most common approach for exports to China
  - Acts only on behalf of head office -- can perform marketing operations, but no actual "selling"
  - Can not import or distribute product itself -- sales from head office to Chinese FTC
- **Manufacturing Joint Venture**
  - Distribute the JV's product in China -- not other products
  - Big investment



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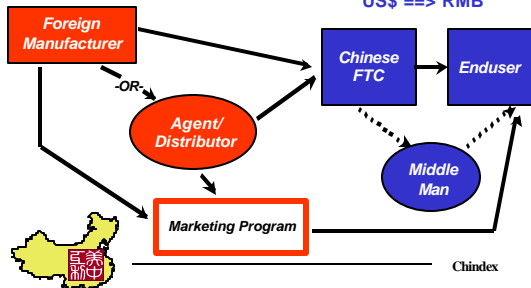
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## Export Distribution Structure

Export - US\$

Import  
US\$ ==> RMB



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## Export Distribution Structure

**Has been effective for capital equipment exports, but the trade regime is restricted**

- All traditional alternatives are very limited in the scope of activities which they allow.
- In the traditional structure, there is no effective legal platform for foreign companies to control the "import"
  - leads to problems, as in 1998:
    - "gray market" imports
    - regulatory Forex crackdown
    - problem with RMB-based collections



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## Consumable Product Imports - The “WFOE-ITC” Platform

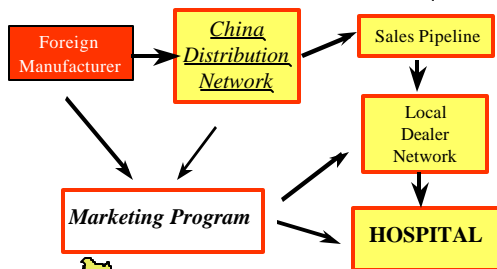
A **Wholly Foreign-Owned Enterprise** operating as an **International Trading Company**...

- Special Economic Zones: Waigaoqiao, Tianjin, etc.
- As a local Chinese company, a “WFOE” business license can provide a platform to establish a physical distribution and financial flows management system
- Multiple “WFOE” operations can provide comprehensive nationwide coverage
- Traditionally a manufacturing venture -- now expanded scope of business license allows for service sector activity



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## Import Distribution Structure: The “WFOE-ITC” Platform



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## Import Distribution Structure: The “WFOE-ITC” Platform

**Allows for management control over the components of successful distribution in China:**

- ▢ Physical Logistics
- ▢ Financial Flows Management
- ▢ Pipeline Management



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## Physical Logistics System

### Key components:

- Legal importation
- Inventory held in China on a regional basis
- RMB sales to local Chinese dealers
- Consistency of supply nationwide

### Critical difficulties:

- Restricted foreign trade regime
- Restricted domestic trade regime
- Underdeveloped infrastructure



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## Financial Flows Management

- **Local currency credit and collections management** is one of the key factors to establishing a predictable, regular, and sustainable supply pipeline.
- A solely US\$-based supply strategy is very limiting for a foreign supplier
  - ❗ if you are waiting for a Letter of Credit to ship your product to China, someone else is selling their product in the meantime



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## Pipeline Management

- **Objective:** regular and growing purchases by an authorized subdealer who is making money selling your product to an established and growing base of end users in their territory
- **Detailed local area management** is the key to insuring that Chinese dealers stay focused and productive
  - product training
  - territorial exclusivity
  - marketing support
  - EU marketing/dealer referrals



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### **Financing US\$ Sales to China**

- If hospital has access to funds, any variety of methods can be utilized in contract with FTC, including L/C or D/P
- If hospital must finance purchase, terms must be “preferential” and competitive with other ECAs
  - Ex-Im Bank loan guarantee w/ buydown
  - Commercial loan w/ buydown



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### **Ex-Im Bank Loan Guarantee**

- Ex-Im will finance up to 85% of contract value
- Remaining 15% must be financed commercially
  - difficult to find banks willing to take on “China risk” if buyer wants terms on 15% to match Ex-Im guaranteed piece
- Foreign content rules apply
  - minimum 50% U.S. content; if between 50-85%, foreign content balance over 15% must be financed outside of Ex-Im guarantee
    - Long-term (>\$10 million or >10 yrs repayment) -- minimum 50% U.S. content **item-by-item**
    - Medium-term -- foreign content determined on **aggregate**



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### **Ex-Im Bank Loan Guarantee vs. Commercial Bank Loan**

- More flexibility with commercial loan -- no foreign content rules, no lengthy approval process
- Commercial bank loan without Ex-Im guarantee is more costly (0.5-1% p.a.)
- Difficult to find a bank to take China risk



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### ***Interest Rate “Buydown”***

- Interest rate provided to Chinese buyer is at a fixed, below market rate
- Interest charged by banks is generally at LIBOR+ (floating rate)
- Difference between market rate charged by bank and rate offered to Chinese buyer is calculated over loan term (including swap) and paid up front by seller



↑ **Acceptable to Ex-Im and buyers but expensive for sellers**

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### ***Ex-Im Bank Direct Loans?***

- Ex-Im offers direct loan programs for U.S. equipment purchases, but:
  - interest rate must be at market rate; “buydown” can not be utilized
  - no initiation of tied aid
  - very difficult to get matching tied aid funding



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